VZCZCXYZ0000
RR RUEHWEB

DE RUEHNC #1600/01 2631327
ZNR UUUUU ZZH
R 201327Z SEP 06
FM AMEMBASSY NICOSIA
TO RUEHC/SECSTATE WASHDC 6888
INFO RUEHTH/AMEMBASSY ATHENS 3667
RUEHLO/AMEMBASSY LONDON 1235
RUEHHE/AMEMBASSY HELSINKI 0376
RUEHBS/USEU BRUSSELS
RUCPDOC/USDOC WASHDC
RUEATRS/DEPT OF TREASURY WASHDC

UNCLAS NICOSIA 001600

SIPDIS

SENSITIVE

SIPDIS

E.O. 12958: N/A
TAGS: EFIN ECON CY
SUBJECT: CYPRUS: BANK OF CYPRUS CHAIRMAN STEPS DOWN AFTER EMPORIKI BANK TAKEOVER FIASCO, SCANDALS; LAIKI BANK PRESIDENT ALSO OUSTED

REF: NICOSIA 1092

(U) This cable is sensitive but unclassified. Please protect accordingly. Not for internet distribution.

¶1. (SBU) Summary. The tumultuous summer for the Cypriot financial sector continued with the Chairmen of Cyprus's two largest banks losing their jobs, despite impressive financial results. On September 1, Vasilis Rologis stepped down in the face of mounting criticism from the Central Bank following the collapse of the BOC's bid to take over Greece's fourth largest bank and several unrelated scandals involving key board allies. On July 26, Kikis Lazarides, Chairman of Laiki Bank, resigned after 30 years at the helm, reportedly under pressure from new minority shareholders Marfin Bank. A potential merger of Laiki with Greek banks Marfin and Egnatia is now in the works. The leadership changes may reflect the Central Bank's efforts to professionalize bank boards -- traditionally viewed as sinecures for the rich and famous -- as Cypriot banks, fully recovered from the stock market crash, find themselves increasingly more attractive targets for foreign investors. End Summary.

Background

¶2. (U) As reported Reftel, the BOC launched a USD 8.2 billion cash-and-shares public offer on June 22 to acquire 100 percent of Emporiki bank - Greece's fourth-largest, but ailing -- bank. If successful, the bid would have turned the combined BOC/Emporiki group into the second-largest financial institution in Greece, with a total market share of 12 percent of deposits and 15 percent of loans. In Cyprus, the BOC enjoys 32 percent of deposits and 27 percent of loans. However, the takeover would have posed a tremendous strain on BOC's capitalization. The bid was seen as a bold move with potential serious consequences for the Cypriot financial system. The success or failure of the takeover would have made or broken the BOC - Cyprus's leading financial institution -- with all the implications that that would have for the Cypriot financial sector.

Saved by the Bell

¶3. (SBU) Many analysts were skeptical from the start about the BOC's ambitious plan to acquire Emporiki. Furthermore, many BOC Board members were openly critical of the plan, citing insufficient information regarding crucial aspects of Emporiki's liabilities. In the end, the skeptics won out. On July 19, the BOC Board of Directors decided unanimously to apply to the Greek Capital Markets Commission to revoke its public tender offer on Emporiki, citing uncertainty regarding Emporiki's pension system. The BOC's back-pedaling came after a Greek court questioned the GOG's plans to

establish a single pension system for all Greek banks, exposing Emporiki's owners to exposure to an additional 600-800 million euro in pension liabilities -- something critics noted any basic due diligence should have discovered.

¶4. (U) The Greek Capital Markets Commission reacted angrily, warning the BOC that, under Greek law, it could withdraw its bid only if (a) its shareholders rejected it; (b) if the Commission itself approves the withdrawal, or (c) if the Central Banks of Greece or Cyprus denied permission for the deal to proceed.

¶5. (U) Just two days later, on July 21, the Central Bank of Cyprus bailed the BOC out by declining to authorize its bid for Emporiki. Had the deal gone through, the BOC's capital adequacy ratio would have declined to 6.4 percent -- well below the 8.0 percent minimum level - directly threatening the viability of the new venture. The BOC's withdrawal left Credit Agricole as the only suitor for Emporiki in Greece. With an improved offer of EUR 25 per share of Emporiki stock, the French bank ended up acquiring 72 percent of Emporiki by July 31.

Rologis Pays with Job

¶6. (SBU) In the aftermath of this debacle, Greek Finance Minister George Alogoskoufis slammed the BOC, saying that its U-turn was "not in line with the seriousness and responsibility required by the (privatization) procedure." A furious Cypriot Central Bank Governor Christodoulou also lambasted the BOC for not conducting due diligence and for failing to carry out the required legal or audit checks. However, one Bank of Cyprus insider told us he thought the hastily-prepared bid was never meant to succeed but was instead intended as a means to discourage a potential take over bid from the Greek Piraeus Bank. In this regard, he noted, it had been successful.

¶7. (SBU) Compounding Rologis's difficulties were a series of scandals that intensified the Central Bank's criticism of Rologis and the BOC and forced the resignation of several of his allies on the board. Board Member and Rologis's ally Polakis Sarris (who is also the cousin of BOC Cypriot operations CEO Charilaos Stavrakis) resigned after the press revealed that the BOC was almost exclusively using his legal firm, paying his company over CYP 1.7 million in fees in 2005. Following public allegations that the BOC was failing to collect on a CYP 1.3 million personal loan to Board member Demetris Pierides, Pierides --- another Rologis ally -- was forced to step down (and a payment plan involving the partial sale of Pierides's massive art collection was quickly announced).

¶8. (SBU) The loss of two critical allies may have tipped the balance against Rologis, who was elected Chairman by the Board in 2005 by a single vote. On September 1, Rologis tendered his resignation as Chairman (but not from the Board), following a major Board battle over policy differences and heavy criticism regarding the handling of the Emporiki bid. Apparently, the massive increase in BOC's expected profits for 2006 (up by 172 percent to around USD 355 million) was not enough to save his job. Under his chairmanship, which began on May 18, 2005, the BOC share price rose from CYP 1.60 to its current level of CYP 4.33. On September 7, the BOC Board elected veteran banker Eleftherios Ioannou, aged 73, as caretaker Chairman until the next BOC shareholders' Annual General Meeting, planned for May 2007. Ioannou had served as the Managing Director of the Greek Alpha Bank's operations in Cyprus from 1990-2000. Ioannou's election was widely regarded as a compromise between Rologis's supporters and opponents.

Fallout Extends Further

¶9. (U) Following the scandals, Central Bank Governor Christodoulou issued a clear public warning to the Boards of banks to clean up their act and cope with the challenges and demands of new EU directives on corporate governance, instead of running banks like family businesses. Christodoulou slammed the practice of regarding banks as "hereditary fiefdoms" and depending on "old boys' networks." The Central Bank Governor also demanded more representative boards and increased transparency in their operations.

¶10. (SBU) The shakedown of senior bank positions in the wake of the failed BOC bid claimed one more casualty at Laiki, Cyprus's second-largest financial institution. Despite impressive results for the first half of 2006, with profits up by 110.7 percent at CYP 38 million, Kikis Lazarides, the once-omnipotent Chairman and CEO of Laiki Bank, who had held that job for over 30 years, tended his resignation on July 26, 2006. Lazarides had made an effort to bow out gracefully a year earlier, in September 2005, when he accepted to stay on as Chairman but without executive powers. However, his disagreements with the Greek financial group Marfin, which has acquired 12 percent of Laiki's stock, finally forced Lazarides to give up control.

¶11. (U) Neoklis Lysandrou, Laiki's most senior General Manager with 34 years of service, was appointed to the board and elected Non-Executive Chairman. In announcing Laiki's new leadership, Marfin Vice President and CEO Andreas Vgenopoulos said, "The Cypriot banking system, though stronger than ever, contains some phenomena of the past decades. Progress will knock down the status-quo and lead to new structures. Structures where the boards are not the chairs for placing one's friends or people who, at some point in time were famous, bestowing them honorary titles. Boards need people with knowledge, an appetite for work, and principles and should be given the opportunity to operate freely for the good of the company."

Laiki/Marfin/Egnatia Merger On Track -- More to Come
-- -------

¶12. (U) Meanwhile, the wave of mergers and acquisitions promising to change the face of Cypriot banking continues. The triple merger between Marfin Bank in Greece, Egnatia Bank also in Greece, and Laiki Bank in Cyprus remains on track. Marfin, which is 31.5 percent owned by Dubai Financial, currently has a 12 percent stake in Laiki and a 40.6 percent stake in Greek bank Egnatia. The boards of the two main players, Marfin and Laiki, approved the overall concept on September 14, and September 19, respectively, although details are still unclear. The merger promises to change the balance of power among domestic banking institutions, creating the largest financial group in terms of capital in Cyprus. The stock of the new entity, which is likely to have a new name, will be traded on three exchanges: Athens, Dubai and Nicosia. The Central Bank of

Cyprus is following developments closely and favors having the new entity headquartered in Cyprus, as opposed to Athens or Dubai. The merger is expected to take place at the end of 2006.

¶13. (U) Following the general trend, the island's third-largest bank, Hellenic, is considering cooperation with other financial institutions that will be of a "complementary nature." Hellenic CEO (and former finance minister) Makis Keravnos recently presented the bank's three-year strategic development plan for 2006 to 2008 and described Hellenic's absence from the Balkans as a "great omission." He also noted that the bank was in contact with banks in Greece, as well as in other new EU members, with a view to pursue these ambitions. Decisions are expected over the next six months.

SCHLICHER